

The slide features a minimalist design with thin grey lines. A vertical line on the left and a horizontal line near the top intersect at a small circle in the upper-left corner. Another horizontal line is positioned below the main title, intersecting a vertical line on the right at a small circle in the lower-right corner. The title 'CONTRACTING PRACTICES' is centered in a large, bold, black, sans-serif font.

# CONTRACTING PRACTICES

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# OVERVIEW OF CONTRACTING PRACTICES

- ◆ Importance of examining contracting trends and practices
- ◆ Trends in contracting between hospitals and payors
- ◆ Evaluation of specific contracting practices

# Why examine contracting practices?

- ◆ Contractual arrangements are the means by which a substantial proportion of healthcare services are purchased and delivered
- ◆ “Contracting” is a primary mechanism by which the terms and conditions of services are determined
- ◆ Contracting practices have changed substantially in recent years

# Contracts as mechanisms

- ◆ Contractual arrangements represent an important mechanism of competition
- ◆ Vital to understand how contracting practices work in “competitive” markets to get a baseline
- ◆ As with any contract, important to consider rationale for contracting practices from both parties’ perspective
  - Payor side
  - Hospital side

# Importance of “contracting”

- ◆ Role and importance of commercial contracts
- ◆ Contracting process
- ◆ Terms and conditions of the contract
  - Complex price and non-price terms
  - Volume commitments
- ◆ Ex ante and ex post assessment of contract profitability – modeling
- ◆ Contract is not a guarantee of “purchases”

# Importance of “contracting”

- ◆ Role and importance of commercial contracts
  - Virtually all commercially insured patients are subject to a form of contractual arrangement between hospital and payor
  - In-network vs. out-of-network
  - Proportion of patients that are commercially insured may vary, but averages above 35% for US hospitals
- ◆ Contract is not a guarantee of “purchases”

# Importance of “contracting”

## ◆ Contracting process

- Substantial amount of time invested by payors and hospitals in initial contract as well as renewal
- Single year versus multi-year

## ◆ Terms and conditions of contract

- Complex price and non-price terms
- Capitated contracts
- Volume commitments

# Importance of “contracting”

- ◆ Ex ante and ex post assessment of contract profitability
  - Modeling
- ◆ Contracting is not a guarantee of purchases

# Trends in contracting

- ◆ Expansion to more inclusive networks
  - Expansion of PPOs
  - Diminished role of exclusive networks
  - Tiered networks
- ◆ Factors that have led to increased “prices” in most markets in recent years
- ◆ Evolution and decline of capitated contracts
  - Buying out of contracts

# Evaluation of “system” contracting

- ◆ Systems as “multi-plant” firms
  - Payors
  - Hospitals
- ◆ Hospital “systems” include a myriad of different structures and types
- ◆ As in any industry, evaluation of contracting practices involves understanding the business rationale for various practices
  - Competitive baseline

# Evaluation of “system” contracting

- ◆ Possible business rationales for aspects of system contracting
  - Common timing of contracts with individual parties or across parties
  - Development and application of “best practices” in contracting provisions
  - Development of more sophisticated IT systems
  - Improved budgeting or understanding of costs associated with delivering healthcare services
  - Possible savings in personnel

# Evaluation of “system” contracting competitive issues

- ◆ Concern has been raised that system contracting may “force” payors to pay supracompetitive prices for some hospital services
- ◆ Distinguishing between all-inclusive network trends and system contracting
- ◆ Evaluate the competitive constraints and mechanisms available to or operating on both parties
  - Practical experience
  - Market conditions
  - Ability of payors to discipline pricing

# Bottom line on contracting practices

- ◆ Important to consider business rationale for specific contracting practices and evolution of contracting practices
- ◆ Need to examine payor side trends and hospital side trends – competitive baseline
- ◆ Competitive effects analysis should take into account competitive constraints and mechanisms available to or operating on both parties